



GOVERNOR'S OFFICE OF
BUDGET AND PROGRAM PLANNING

Fiscal Note 2009 Biennium

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|-------------------------|---------------|----------------|--|
| Bill # | HB0824 | Title: | Exempt military pensions from state income tax |
| Primary Sponsor: | Ingraham, Pat | Status: | As Amended |

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|---|--|--|
| <input type="checkbox"/> Significant Local Gov Impact | <input type="checkbox"/> Needs to be included in HB 2 | <input type="checkbox"/> Technical Concerns |
| <input type="checkbox"/> Included in the Executive Budget | <input type="checkbox"/> Significant Long-Term Impacts | <input type="checkbox"/> Dedicated Revenue Form Attached |

FISCAL SUMMARY

| | <u>FY 2008 Difference</u> | <u>FY 2009 Difference</u> | <u>FY 2010 Difference</u> | <u>FY 2011 Difference</u> |
|---|--------------------------------------|--------------------------------------|--------------------------------------|--------------------------------------|
| Revenue: | | | | |
| General Fund | (\$6,448,337) | (\$6,512,474) | (\$6,577,477) | (\$6,643,347) |
| Net Impact-General Fund Balance: | <u>(\$6,448,337)</u> | <u>(\$6,512,474)</u> | <u>(\$6,577,477)</u> | <u>(\$6,643,347)</u> |

Description of fiscal impact:

Beginning in 2007, this bill would exempt the first \$15,000 of military pension income from the income tax. This would reduce general fund revenue by about \$6.5 million per year.

FISCAL ANALYSIS

Assumptions:

1. This bill would exempt the first \$15,000 of a taxpayer's military pension from the income tax, effective January 1, 2007. Under current law, the first \$3,600 of retirement income is exempt for taxpayers with federal adjusted gross income less than \$30,000, with the exemption phasing out by about \$31,800, depending on the taxpayer's pension and other income. The exemption in this bill would be in addition to the existing exemption.
2. In 2005, there were 7,293 veterans in Montana receiving retirement pay. They received a total of \$136,776,000, an average of \$18,754 per recipient.
3. A military retiree's initial retirement payments depend on the retiree's grade at retirement and years of service. The minimum initial pension for a service member retiring with 20 years of service in 2007 is \$12,377. (Department of Defense online retirement calculator <http://www.dod.mil/cgi-bin/finalpayhigh3.pl>) Most military retirees will be receiving higher pensions. Retirement payments are subject to annual escalation.

4. Military retirees with total pension income of more than \$18,600 or federal adjusted gross income of more than \$31,800 will have \$15,000 of military pension income exempted. Of all returns with more retirement income than the minimum military pension, 86.3% have total pension income greater than \$18,600 or federal adjusted gross income greater than \$31,800. However, the average military pension is less than average pension income for all taxpayers with pension income higher than the minimum military pension. Therefore, this fiscal note assumes that 80% of military retirees in Montana will receive the full additional exemption of \$15,000 and that the average additional exemption for the other 20% is \$13,700.
5. The number of military retirees is assumed to grow 1% per year. The number of retirees in Montana will be 7,440 in 2007, 7,514 in 2008, 7,589 in 2009, and 7,665 in 2010.
6. This bill would exempt military pensions of \$109,665,600 in 2007 ($80\% \times 7,440 \times \$15,000 + 20\% \times 7,440 \times \$13,700$), \$110,756,360 in 2008 ($80\% \times 7,514 \times \$15,000 + 20\% \times 7,514 \times \$13,700$), \$111,861,860 in 2009 ($80\% \times 7,589 \times \$15,000 + 20\% \times 7,589 \times \$13,700$), and \$112,982,100 in 2010 ($80\% \times 7,665 \times \$15,000 + 20\% \times 7,665 \times \$13,700$).
7. Most military pension recipients have other income or have pensions of more than \$15,000. Thus, the reduction in tax revenue can be calculated by multiplying the income reduction by the marginal tax rate, which is the rate the taxpayer pays on an increment of income. The average marginal tax rate of taxpayers with pension income is 5.88%. This bill will reduce income tax liability by \$6,448,337 in 2007 ($5.88\% \times \$109,665,600$), \$6,512,474 in 2008 ($5.88\% \times \$110,756,360$), \$6,577,477 in 2009 ($5.88\% \times \$111,861,860$), and \$6,643,347 in 2010 ($5.88\% \times \$112,982,100$).
8. The impact on revenue will show up as larger refunds and smaller payments with returns when taxpayers file their returns the spring following each tax year. General fund revenue will be reduced in FY 2008 through FY 2011 by the amounts calculated in assumption 7 for tax years 2007 through 2010.
9. This bill would not affect the Department of Revenue's costs of administering the individual income tax.

| | <u>FY 2008</u> <u>Difference</u> | <u>FY 2009</u> <u>Difference</u> | <u>FY 2010</u> <u>Difference</u> | <u>FY 2011</u> <u>Difference</u> |
|---|---|---|---|---|
| <u>Fiscal Impact:</u> | | | | |
| <u>Revenues:</u> | | | | |
| General Fund (01) | (\$6,448,337) | (\$6,512,474) | (\$6,577,477) | (\$6,643,347) |
| TOTAL Revenues | (\$6,448,337) | (\$6,512,474) | (\$6,577,477) | (\$6,643,347) |
| <u>Net Impact to Fund Balance (Revenue minus Funding of Expenditures):</u> | | | | |
| General Fund (01) | (\$6,448,337) | (\$6,512,474) | (\$6,577,477) | (\$6,643,347) |

Long-Range Impacts:

1. The revenue reduction will grow over time as military pension income grows.

*Sponsor's Initials*_____
*Date*_____
*Budget Director's Initials*_____
Date